The Manitoba Hydro-Electric Board

Quarterly Report

for the six months ended
September 30, 2016

Comments by **The Chair of the Board** and by **The President and Chief Executive Officer**

Financial Overview

Manitoba Hydro's consolidated net loss was $70 million for the first six months of the 2016-17 fiscal year compared to a net loss of $17 million for the same period last year. The increase in the net loss is primarily attributable to higher expenses such as finance costs, capital taxes and depreciation.

The consolidated net loss was comprised of a $51 million loss in the electricity segment, a $24 million loss in the natural gas segment and a $5 million net profit in other segments.

The loss in both the electric and natural gas sectors is expected to be recouped over the winter heating season. Manitoba Hydro is forecasting that financial results will improve over the balance of the fiscal year and net income is forecast to reach approximately $25 million by March 31, 2017. This forecast is based on the continuation of current water flow and export market conditions and the assumption of normal winter weather.

Electric Segment

Revenues from electricity sales within Manitoba totaled $622 million for the six-month period, which was $2 million or 0.3% higher than the same period last year. The increase in domestic revenue was primarily attributable to the electricity rate increase effective August 1, 2015 as well as customer growth partially offset by lower customer usage and lower weather-related consumption. Extraprovincial revenues of $246 million were $2 million or 0.8% higher than the same period last year reflecting higher dependable sales volumes partially offset by lower export prices on opportunity sales. Energy sold in the export market was 6.3 billion kilowatt-hours compared to 6.2 billion kilowatt-hours sold in the same period last year. Other revenues of $13 million were $3 million or 19% lower than the same period last year primarily due to the recognition of interconnection study revenue in the prior year.

Expenses attributable to electricity operations, including the net movement in regulatory deferral balances, totaled $938 million for the six-month period, an increase of $53 million or 6% higher than the same period last year. The increase was primarily the result of a $29 million increase in net finance expense, an $8 million increase in capital and other taxes, a $6 million increase in depreciation and amortization expense, a $5 million increase in fuel and power purchased and a $4 million increase in operating and administrative expenses. The increase in net finance expense was primarily as a result of the impact of the weakening Canadian dollar resulting in realized foreign exchange losses on U.S. debt.

In addition, there were higher volumes of long-term debt to finance capital expenditures, partially offset by lower interest rates. Capital and other taxes increased as a result of additional debt borrowings required for major capital development. The increase in depreciation and amortization is primarily attributable to new additions to plant being placed into service including the earth filled dam associated with the Pointe du Bois spillway replacement. The increase in fuel and power purchases is primarily due to an increase in U.S. transmission rates as well as additional dependable wind purchases resulting from higher wind generation. The increase in operating and administrative costs is mainly due to higher wages, salaries and benefits, partially offset by increased deployment of staff to capital projects and staffing reductions.

The net loss before net movement in regulatory balances is $85 million. After considering the net movement of $28 million in the regulatory deferral balances, there is a net loss of $57 million of which $51 million is attributable to Manitoba Hydro and $6 million is attributable to non-controlling interest. The non-controlling interest represents Taskinigahp Power Corporation's 33% share of the Wuskwatim Power Limited Partnership's operating results, for the first six months of the 2016-17 fiscal year.

Expenditures for capital construction for the six-month period amounted to $1 347 million compared to $1 001 million for the same period last year. Expenditures for the current period included $535 million related to construction of the Keeyask project and $526 million for the Bipole III reliability project. The remaining capital expenditures were incurred for ongoing system additions and modifications necessary to meet the electrical service requirements of customers throughout the province. The corporation also incurred $19 million for electric Power Smart programs.

Natural Gas Segment

The net loss in the natural gas segment was $24 million for the six-month period compared to a $25 million net loss for the same period last year. Revenue, net of cost of gas sold (net revenue), was $54 million which was $12 million higher than the same period last year. The increase in net revenue was largely the result of lower gas and transportation costs compared to the same period in the prior year. Delivered gas volumes were 609 million cubic metres compared to 564 million cubic metres for the same period last year.

Expenses attributable to natural gas operations excluding cost of gas sold amounted to $73 million which is comparable to the same period last year.

The net loss before net movement in regulatory balances is $19 million. The $12 million change in net movement of the regulatory deferral balances over the prior year is primarily attributable to a greater differential between actual cost of gas and transportation costs compared to the Public Utilities Board (PUB) approved rates. After considering the net movement of $5 million in the regulatory balances, there is a net loss of $24 million.

Capital expenditures in the natural gas segment were $26 million for the current six-month period compared to $18 million for the same period last year. Capital expenditures are related to system improvements and other expenditures necessary to meet the natural gas service requirements of customers throughout the province. The corporation also incurred $4 million for gas Power Smart programs.

Other Segments

The other segments include Manitoba Hydro International Ltd., Manitoba Hydro Utility Services, Minell Pipelines Ltd. and Teshmont Holdings Ltd. The net income was $3 million in other segments for the six-month period compared to net income of $5 million for the same period last year. Revenue was $30 million which was $2 million lower than the prior period. Expenses attributable to other segments amounted to $27 million which is comparable to the same period last year.

There is also a $2 million profit impact in adjustments and eliminations as a result of the requirement to harmonize accounting policies between electric and gas operations related to the gas meter exchange program.

Electricity Rate Increase

Electricity rates for all customer classes increased by 3.36% effective August 1, 2016. The increase will result in a $2.83 increase in the monthly bill of a typical residential customer without electric heating, using an average of 1 000 kilowatt hours per month. Customers with electric heating, using an average of 2 000 kilowatt hours per month, will see a monthly increase of approximately $5.41.

The PUB directed that all additional revenue generated from this rate increase be added to the previously established deferral account to mitigate rate increases when the Bipole III reliability project comes into service.

Natural Gas Rate Increase

In accordance with Manitoba Hydro's methodology to change natural gas rates every quarter depending on the price of gas purchased from Alberta, rates for residential customers increased on August 1, 2016, by 6.5% or approximately $49 per year. Rate changes for larger volume customers ranged from increases of 7.6% to 15.2% depending on the customer class and consumption levels.

The bill impacts are primarily the result of changes in the price that Manitoba Hydro pays for natural gas from Alberta.

Manitoba Hydro-Electric Board Releases Review

On September 21, 2016, the Manitoba Hydro-Electric Board (MHEB) released its review conducted at the request of the Government of Manitoba. Although the review began with a primary focus on Bipole III, it quickly expanded in scope to include the Keeyask Generating Station, Manitoba Hydro's capital program and ultimately, the overall financial situation and operation of Manitoba Hydro.

To assist with its work, the MHEB retained the Boston Consulting Group, an acknowledged world-class industry expert in utility operations, finance and major projects, to provide independent analysis and support.

The review concluded that re-routing or cancelling Bipole III at this stage is not a viable option, nor is cancelling Keeyask. Therefore, Manitoba Hydro must move forward with completing the projects. The review also concluded the decisions to build the Bipole III, Keeyask and the Manitoba-Minnesota Transmission Project (MMTP) concurrently will see Manitoba Hydro's debt increase to $25 billion in the next three to four years which will place strain on the utility's finances.

The MHEB review identified that the cost for Bipole III could rise from the current budget of $4.65 billion to between $4.9 and $5 billion and that the project's completion may be delayed by 12 to 15 months. The Keeyask project could experience a delay of between 21 and 31 months, and could see costs rise from the current budget of $6.5 billion to between $7.2 and $7.8 billion.

Manitoba Hydro management with support from the MHEB is planning to move forward with completing the projects with minimal delay and the least possible incremental cost.

The MHEB concluded that Bipole III is essential to reducing the significant risk of blackouts and service disruptions should there be a failure of the existing Bipole I and Bipole II transmission lines, which currently deliver more than 70 per cent of the electricity produced in the province.

The MHEB also concluded that construction of the Keeyask Generating Station and MMTP must proceed as it would jeopardize export contracts worth $4.5 billion.

Manitoba Hydro's executive, with advice and guidance from the MHEB, is working diligently on the preparation of a plan to address the corporation's financial challenges.

Manitoba Hydro Expands Power Smart Rebates

On September 30, 2016 Manitoba Hydro Power Smart® expanded its fall instant rebate promotion to include a host of new energy-saving technologies, in addition to the ever-popular LED bulbs.

The province-wide promotion now offers instant rebates, through participating retailers, on LED fixtures, lighting controls, smart power bars, plug-in timers, low-flow showerheads, weather-stripping and window insulating film kits.

Until January 31, 2017, customers can also receive a Manitoba Hydro bill credit for the purchase of a "smart thermostat" and/or ENERGY STAR® certified washing machine or washer/dryer pair. Customers can purchase eligible products from any retailer of their choice, or buy online, and then visit Manitoba Hydro's website to apply for their rebate.

Since the first LED rebate program launched in the fall of 2014, more than 85 000 households have purchased ENERGY STAR® certified LED bulbs, saving approximately $3.6 million a year on their electricity bills. LED bulbs use 80 per cent less energy than incandescent lights.

The fall Power Smart campaign has proven to be one of Manitoba Hydro's most successful and popular promotions with residential customers.

New Natural Gas Line Improves Reliability

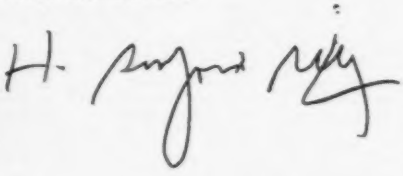
The Northwest Winnipeg Natural Gas Project is one of the largest natural gas pipeline projects in Manitoba since the early 1960s. The project is designed to meet increasing demand for natural gas service north of Winnipeg. It involves approximately 60 kilometres of pipeline installed along a route that runs next to the west Perimeter Highway north to Highway 6, and along Provincial Road 236 to Selkirk.

The new pipeline includes tie-ins to existing pipelines at Stonewall and Selkirk. Work on the $28 million project began about two years ago and is expected to be in-service by the end of 2016.

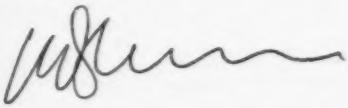
The project provides additional flexibility in the overall Winnipeg-area gas-transmission network as it helps maintain the security of gas supply to customers in the event of damage to one of the gas transmission lines supplying Winnipeg. Importantly, the new pipeline will also permit existing pipelines to be taken out of service for inspection during periods of lighter load.

Manitoba Hydro delivers natural gas to 276 858 customers in nearly 100 communities across southern Manitoba. In an average year, Hydro delivers about 2.1 billion cubic metres of natural gas throughout the system.

H. Sanford Riley
Chair of the Board



Kelvin Shepherd, P. Eng.
President and
Chief Executive Officer
November 14, 2016



Consolidated Statement of Income

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		Three Months Ended September 30	
	2016	**2015**	**2016**	**2015**
Revenues				
Domestic – Electric	622	620	310	310
– Gas	95	97	36	37
Extraprovincial	246	244	141	133
Other	39	43	18	22
	1 002	1 004	505	502
Expenses				
Cost of gas sold	42	56	19	23
Operating and administrative	302	298	148	148
Finance expense (net)	314	285	155	142
Depreciation and amortization	203	196	102	97
Water rentals and assessments	62	61	31	30
Fuel and power purchased	62	57	31	31
Capital and other taxes	69	62	34	32
Other expenses	47	49	26	27
	1 101	1 064	546	530
Net loss before net movement in regulatory balances	(99)	(60)	(41)	(28)
Net movement in regulatory balances	23	37	17	24
Net Loss	(76)	(23)	(24)	(4)
Net loss attributable to:				
Manitoba Hydro	(70)	(17)	(22)	(1)
Non-controlling interest	(6)	(6)	(2)	(3)
	(76)	(23)	(24)	(4)

Consolidated Statement of Financial Position

In Millions of Dollars (Unaudited)

	As at September 30	As at September 30
	2016	**2015**
Assets		
Current assets	1 587	918
Property, plant and equipment	18 389	16 075
Non-current assets	660	827
Total assets before regulatory deferral balance	20 636	17 820
Regulatory deferral balance	516	447
	21 152	18 267
Liabilities and Equity		
Current liabilities	962	1 285
Long-term debt	15 833	12 895
Other long-term liabilities	1 594	1 524
Deferred revenue	579	483
Non-controlling interest	155	131
Retained earnings	2 757	2 762
Accumulated other comprehensive loss	(786)	(836)
Total liabilities and equity before regulatory deferral balance	21 094	18 244
Regulatory deferral balance	58	23
	21 152	18 267

Consolidated Cash Flow Statement

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		*Three Months Ended September 30*	
	2016	**2015**	**2016**	**2015**
Operating Activities				
Cash receipts from customers	1 099	1 115	539	516
Cash paid to suppliers and employees	(488)	(542)	(58)	(292)
Net interest	(350)	(334)	(179)	(177)
	261	239	302	47
Financing Activities	1 286	743	712	351
Investing Activities	(1 423)	(1 095)	(850)	(557)
Net increase (decrease) in cash	124	(113)	164	(159)
Cash at beginning of period	956	494	916	540
Cash at end of period	1 080	381	1 080	381

Consolidated Statement of Comprehensive Loss

In Millions of Dollars (Unaudited)

	Six Months Ended September 30		*Three Months Ended September 30*	
	2016	**2015**	**2016**	**2015**
Net Loss attributable to Manitoba Hydro	(70)	(17)	(22)	(1)
Other Comprehensive Income (Loss)				
Items that will be reclassified to income				
Unrealized foreign exchange gains (losses) on debt in cash flow hedges	(20)	(107)	(15)	(138)
Items that have been reclassified to income				
Realized foreign exchange (gains) losses on debt in cash flow hedges	10	(9)	5	(5)
	(10)	(116)	(10)	(143)
Comprehensive Loss attributable to Manitoba Hydro	(80)	(133)	(32)	(144)

Segmented Information

In Millions of Dollars (Unaudited)

	Electric Segment		Natural gas segement		All other segments		Eliminations		Total	
Six Months Ended September 30	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**
Revenue	881	880	95	97	30	32	(4)	(5)	1 002	1 004
Expenses	966	915	114	129	27	27	(6)	(7)	1 101	1 064
Net income (loss) before net movement in regulatory balances	(85)	(35)	(19)	(32)	3	5	2	2	(99)	(60)
Net movement in regulatory balances	28	30	(5)	7	-	-	-	-	23	37
Net Income (Loss)	(57)	(5)	(24)	(25)	3	5	2	2	(76)	(23)
Net income (loss) attribute to:										
Manitoba Hydro	(51)	(1)	(24)	(25)	3	5	2	2	(70)	(17)
Non-controlling interest	(6)	(6)	-	-	-	-	-	-	(6)	(6)
	(57)	(5)	(24)	(25)	3	5	2	2	(76)	(23)
Three Months Ended September30										
Revenue	456	451	36	37	15	17	(2)	(3)	505	502
Expenses	481	460	55	60	13	14	(3)	(4)	546	530
Net income (loss) before net movement in regulatory balances	(25)	(9)	(19)	(23)	2	3	1	1	(41)	(28)
Net movement in regulatory balances	14	17	3	7	-	-	-	-	17	24
Net Income (Loss)	(11)	8	(16)	(16)	2	3	1	1	(24)	(4)
Net income (loss) attribute to:										
Manitoba Hydro	(9)	11	(16)	(16)	2	3	1	1	(22)	(1)
Non-controlling interest	(2)	(3)	-	-	-	-	-	-	(2)	(3)
	(11)	8	(16)	(16)	2	3	1	1	(24)	(4)
Total assets	20 621	17 748	673	680	76	69	(218)	(230)	21 152	18 267

Generation and Delivery Statistics

	Six Months Ended September 30		*Three Months Ended September 30*	
	2016	**2015**	**2016**	**2015**
Electricity in gigawatt-hours				
Hydraulic generation	17 291	17 202	8 815	8 654
Thermal generation	19	16	17	16
Scheduled energy imports	11	22	8	13
Wind purchase (MB)	434	405	184	193
Total system supply	17 755	17 645	9 025	8 876
Gas in millions of cubic metres				
Gas sales	264	248	81	79
Gas transportation	345	316	165	138
	609	564	246	217

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For further information contact:

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